Supreme Court of the United States

October Term, 1937

No. 641

J. D. ADAMS MANUFACTURING COMPANY,
Appellant,

vs.

WILLIAM STOREN, as Chief Administrative Officer of The Department of Treasury of the State of Indiana, et al.,
Appellees.

APPEAL FROM THE SUPREME COURT OF THE STATE OF INDIANA

BRIEF FOR APPELLANT

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CITATIONS

Cases:

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No. 641

J. D. Adams Manufacturing Company,
Appellant,

vs.

William Storen, as Chief Administrative Officer of The Department of Treasury of the State of Indiana; Department of Treasury of the State of Indiana; Paul V. McNutt, William Storen, Floyd E. Williamson, as and constituting The Board of Department of Treasury of the State of Indiana; Philip Lutz, Jr., as Attorney General of the State of Indiana,
Appellees.

On Appeal From the Supreme Court of the State of Indiana

BRIEF FOR APPELLANT

The Opinions Below

The majority and dissenting opinions of the Supreme Court of Indiana are not yet officially reported. Both

opinions are to be found in 7 N. E. (2d) 941, also in the Record, pp. 43, 61, and Appendix A in the Statement as to Jurisdiction.

Jurisdiction

Paragraph 1 of Rule 12 of the rules of this Court has been complied with, and probable jurisdiction noted by this Court on January 10, 1938.

Questions Presented

The questions presented for decision in this case are:

1. Whether the gross income tax law of Indiana as applied to gross receipts derived from interstate and foreign commerce lays an illegal burden on such commerce and an impost or duty upon exports under Article I, Section 8 and Section 10 of the Federal Constitution; and

2. Whether said law as applied to gross receipts of interest from Indiana tax-exempt bonds constitutes an impairment of the obligation of contract under Article I, Section 10 of the Federal Constitution.

The Statute Involved

The statute involved is the "Gross Income Tax Act of 1933," Ch. 50, Indiana Acts 1933, p. 388; Ind. Stat. Ann. (Burns) 1933, Sec. 64-2601, et seq. The pertinent provisions of the Act will be found in the Appendix A, *infra,* pp. 55-60.

Statement

The facts in the case were stipulated, the trial court made findings thereon, and judgment was entered in favor

of appellant* on all questions raised in the complaint (R. 16-21). Certain points not contested on appeal in the state Supreme Court or involving construction of the statute alone are not presented here. The facts set forth in the stipulation and findings, so far as pertinent on this appeal, may be summarized as follows:

Appellant is an Indiana corporation engaged in manufacturing machinery and equipment for the construction and repair of highways (R. 25, 17). Its home office, principal place of business and only manufacturing plant are at Indianapolis, Indiana (R. 25, 17). It pays state and local taxes on its real and personal property located in the State, and the tax on gross receipts here involved is in addition thereto (R. 25). Approximately eighty per cent (80%) of its products are sold to customers in states other than Indiana and in foreign countries (R. 28, 17). All sales made to customers located outside the State of Indiana are upon orders taken subject to approval of the home office (R. 26, 17). Shipments are made from the factory, and payments made to and received at the home office (R. 26, 17). Receipts from business in other states and foreign countries for each of the four years preceding the trial were in excess of One Million Dollars ($1,000,000), and substantial specific sales were made in other states and foreign countries subsequent to May 1, 1933, effective date of the Act, and before the complaint was filed, and cash had

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*Note:—J. D. Adams Mfg. Co. was plaintiff in the trial court, appellee in the state Supreme Court, and is appellant in this Court. William Storen et al. were defendants in the trial court, appellants in the state Supreme Court, and are appellees in this Court.

In this brief (excepting quotations), "appellant" always refers to J. D. Adams Mfg. Co.; "appellees" always refers to William Storen et al.

been received in payment therefor (R. 26, 27). It was estimated that gross receipts of appellant from the sales of its products in interstate and foreign commerce would continue to be a substantial portion of its entire gross income each year (R. 28-29).

Prior to date of passage of the Act, appellant had acquired, and on the effective date of the Act had in its possession, bonds and other obligations issued by municipal corporations of the State of Indiana in excess of Two Hundred Thousand Dollars ($200,000) face value (R. 29, 18). Such obligations at the time of their issuance were declared by statute to be exempt from taxation (R. 29, 18). Subsequent to May 1, 1933, and before filing the complaint, appellant had collected and received as interest earned on such tax-exempt obligations in excess of Two Thousand Five Hundred Dollars ($2,500) (R. 29).

Before the suit was brought, appellees, as authorized taxing officials of the State, were asserting the right and had declared their determination to impose the tax upon all gross receipts of appellant and others similarly situated derived from sales in interstate and foreign commerce and upon all gross receipts derived from interest on tax-exempt bonds of municipal corporations of the State of Indiana, and to take all steps necessary to collect the same (R. 34-35).

An actual controversy existed between appellant in its own behalf and in behalf of other taxpayers similarly situated and the appellees; and it was necessary that the rights, status and legal relations of the parties in respect to the subject-matter of the suit be determined and declared by the court, and the parties were entitled to have their respective rights under the various provisions of the Gross Income Tax Act of 1933 declared by the court, pur-

suant to the provisions of the uniform declaratory judgments act of Indiana (R. 35, 16-17).

Under the statute, by construction of the state court, the tax is applied to the gross receipts* of appellant at the following rates: upon receipts from sales of products to ultimate users at the rate of one per cent (7 N. E. (2d). 943); upon receipts from sales of products to persons who resell at the rate of one-fourth of one per cent (7 N. E. (2d) 943); and upon receipts of interest from tax-exempt bonds at the rate of one per cent (R. 79).

Specification of Errors to be Urged

The errors of the court below will be urged as to both phases of the case as set forth in appellant's Assignment of Errors (R. 70-71), and may be summarized as follows:

First: That the Supreme Court of Indiana erred in holding that the Gross Income Tax Act of 1933 may be applied to gross receipts derived from interstate and foreign commerce without constituting an undue regulation of and burden upon such commerce, or an impost or duty upon exports without the consent of Congress, in violation of Article I, Section 8 and Section 10 of the Constitution of the United States.

Second: That the Supreme Court of Indiana erred in holding that the Gross Income Tax Act of 1933 may be applied to gross receipts of interest from tax-exempt bonds

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*Note.—In this brief, the terms "gross receipts" and "gross income" are used interchangeably. The 1933 statute is called a "Gross Income Tax Act," but under Section 1 (f), gross income is defined to be "gross receipts." The tax is levied upon "gross earnings" only of certain classes of taxpayers (Section 1 (g), but as to appellant and others similarly situated, it is laid on gross receipts (Regulation 6; R. 76).

of Indiana municipal corporations issued before the effective date of the Act without impairing the obligation of contracts in violation of Article I, Section 10 of the Constitution of the United States.

Summary of Argument

I

Burden on Interstate and Foreign Commerce

The Indiana Gross Income Tax Act of 1933 as construed and applied by the state Supreme Court imposes a tax upon the entire proceeds from sales by all manufacturers, wholesalers and merchants operating in the State, including proceeds from goods sold and shipped to points outside the State. The rate of tax is one per cent or one-fourth of one per cent of the gross receipts, depending on whether the sale is at wholesale or retail. The tax must be paid quarterly. This tax is in addition to all ad valorem property taxes as well as other excise taxes. The tax when laid upon gross receipts from interstate and foreign commerce amounts to a regulation of and a direct burden upon such commerce. The State exacts for its own use a certain percentage of the entire proceeds from all interstate and foreign commerce. The effect upon such commerce is not remote, but is direct and immediate. The burden so imposed must unavoidably be considered a regulation of and restraint upon such commerce in conflict with the Federal Constitution. It is immaterial what the nature of the tax is. Whether it is laid on the privilege of manufacturing, or the privilege of merchandising, or the right to receive gross income, or upon gross receipts as such, the result is the same. The effect is to impose a tax upon the privilege of engaging in interstate commerce, or upon such commerce itself, which the State may not do. The tax would be no less a burden on interstate commerce

even if it were of general application and non-discriminatory character. It is the sort of tax in all respects which this Court has consistently held to be in violation of the commerce clause in the line of decisions which are referred to later in this brief.

II

Impairment of Contract

Article I, Section 10 of the Constitution of the United States provides that no state shall pass any "law impairing the obligation of contracts."

On May 1, 1933, the Gross Income Tax Act of 1933 became effective. The Act levies a tax upon gross receipts from various sources. By Regulation No. 62 of the Department of Treasury (R. 92) and decision of the Supreme Court in this case (7 N. E. (2d) 943), the tax has been applied to all interest derived from municipal securities. Receipts of interest from bonds of Indiana municipal corporations issued prior to the effective date of the Act have been included in the class taxed, even though such bonds were issued under a statute expressly declaring them to be exempt from taxation (Ch. 191, Sec. 1 (twentieth), Indiana Acts 1923, p. 562), which it is conceded constitutes a contract with the bondholder (R. 29; 7 N. E. (2d) 944). Appellant is the owner of bonds of Indiana municipal corporations issued prior to the effective date of the Gross Income Tax Act under the statute declaring them to be tax exempt. Appellant contends that since the Act takes one per cent of all the interest received by the appellant from such tax-exempt securities, the securities themselves are taxed and the contract of exemption is impaired within the meaning of the Constitution of the United States. *Northwestern Mutual Life Insurance Co. v. Wisconsin*, 275 U. S. 136.

ARGUMENT

I

The Tax is Invalid as Applied to Gross Receipts from Interstate and Foreign Commerce

Appellant is engaged in the manufacture of certain products. It is also engaged in the merchandising of those products. There is no gain from manufacture alone. The products must be sold. Appellant's goods after manufacture are traded and exchanged for their equivalent in money. That is commerce.[1] By far the greater part of such goods are sold in other states and in foreign countries. That is interstate commerce. The statute in question here purports to impose a tax upon gross income received in the State of Indiana from all sources. As construed by the state Supreme Court, it requires a tax to be laid on all gross receipts of appellant and others similarly situated, including those derived from the sale of products in interstate and foreign commerce. Returns and payment must be made quarterly. This tax is in addition to the usual ad valorem property taxes, state and local. In computation of the tax, gross receipts from business done in interstate and foreign commerce are readily separable from gross receipts from business transacted within the State,[2] and the Gross Income Tax Division of the Depart-

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[1].—*Brown v. Maryland,* 12 Wheat. 419, 446-447; *Welton v. Missouri,* 91 U. S. 275, 280; *Kidd v. Pearson,* 128 U. S. 1, 20-21; *Addyston Pipe & Steel Co. v. United States,* 175 U. S. 211, 241-242; *Adair v. United States,* 208 U. S. 161, 176-177; *Real Silk Hosiery Mills Inc. v. Portland,* 268 U. S. 325; *Carter v. Carter Coal Co.,* 298 U. S. 238, 297-298.

[2].—*Ratterman v. Western Union Telegraph Co.,* 127 U. S. 411, 424, 427; *Bowman v. Continental Oil Co.,* 256 U. S. 642, 646-647.

ment of Treasury has recognized this by providing separate forms of returns (Reg. 193, R. 144-145, and Regulation 3801, Appendix B, Statement as to Jurisdiction).

A mercantile transaction in interstate commerce consists in (a) selling and shipping the goods, and (b) receiving the pay. The second is inseparable from the first. There could be no interstate commerce without payment for the goods sold and shipped. The very object of engaging in commerce is to receive pay for it.[3] So a tax upon the receipts from sales in interstate commerce is incontrovertibly a tax upon interstate commerce. It is a burden on interstate commerce, and the burden is direct. There can be no conception of anything in the nature of a tax that would be a more direct burden upon such commerce.

The theory of the tax is immaterial—whether conceived to be a tax upon gross receipts as such, or upon the right to take such receipts, or upon the actual taking of such receipts, or upon the privilege of manufacturing the goods, or upon the privilege of merchandising the goods, the effect is the same. The State exacts for itself a certain percentage out of every dollar received in payment for the goods sold and shipped. The amount of the tax fluctuates with the volume of receipts from such commerce, and is at all times directly related to it. The tax, being upon *gross receipts*, as distinguished from *net income*,[4] is upon the price and consideration received for the goods, is imposed directly on the commerce, and is a direct burden on the commerce itself. Whether the tax be considered as laid upon gross receipts or as laid on interstate commerce itself, no distinction can be discerned between the two. A tax on

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[3].—*Phila. & S. M. S. S. Co. v. Pennsylvania,* 122 U. S. 326, 337-338.

[4].—*United States Glue Co. v. Oak Creek,* 247 U. S. 321, 328-329.

gross income or receipts from interstate commerce is in truth a tax upon the engaging in interstate commerce. It cannot be otherwise. While a state may tax the privilege of engaging in local business, it may not tax the privilege of engaging in interstate commerce.[5] Taxation being one of the forms of regulation under Article I, Section 8 of the Federal Constitution, any tax directly laid upon such privilege is void even in the absence of legislation by Congress or a finding of prejudice or discrimination.[6] The selling and shipping of merchandise from Indiana into other states and foreign countries being interstate or foreign commerce, the State "is not at liberty to tax the privilege of doing it by exacting in return therefor a percentage of the gross receipts. Decisions to that effect are many and controlling."[7]

As applied by the Court below to gross receipts from interstate commerce, the tax here involved is of a type which this Court in a line of decisions unbroken for more than half a century has held to be an unconstitutional burden on interstate commerce.

Phila. & S. M. S. S. Co. v. Pennsylvania, 122 U. S. 326;

Leloup v. Port of Mobile, 127 U. S. 640;

Galveston, H. & S. A. R. Co. v. Texas, 210 U. S. 217;

Meyer v. Wells, Fargo & Co., 223 U. S. 298;

Crew Levick Co. v. Pennsylvania, 245 U. S. 292;

Cudahy Packing Co. v. Minnesota, 246 U. S. 450;

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[5].—*East Ohio Gas Co. v. Tax Commission,* 283 U. S. 465, 470; *Cooney v. Mountain States Tel. & Tel. Co.,* 294 U. S. 384, 392; *Pacific Tel. & Tel. Co. v. Tax Commission,* 297 U. S. 403, 412-413.

[6].—*Pacific Tel & Tel. Co. v. Tax Commission,* 297 U. S. 403, 412-413.

[7].—*Puget Sound Stevedoring Co. v. Tax Commission,* 82 L. Ed. advance paging 66.

United States Glue Co. v. Oak Creek, 247 U. S. 321;
Sprout v. South Bend, 277 U. S. 163, 171;
New Jersey Bell Tel. Co. v. State Board, 280 U. S. 338, 349;
Cooney v. Mountain States Tel. & Tel. Co., 294 U. S. 384, 392-393;
Matson Navigation Co. v. State Board, 297 U. S. 441, 444;
Pacific Tel. & Tel. Co. v. Tax Commission, 297 U. S. 403, 412-413;
Fisher's Blend Station v. Tax Commission, 297 U. S. 650, 655-656;
Puget Sound Stevedoring Co. v. Tax Commission, 82 L. Ed. advance paging 64.
(See also, *Dissenting Opinion* by Treanor, J., in the instant case, 7 N. E. (2d) 941, 951; Statement as to Jurisdiction, p. 42; and R. 61.)

In full accord with the decisions of this Court is also a prior decision of the Indiana Supreme Court. There in a carefully considered opinion, after referring to and discussing a number of the earlier decisions of this Court, it was said:

> "Under the law, as authoritatively declared by the court of last resort, no tax, in any form, or for any purpose, can be laid upon interstate commerce. The matter of interstate commerce is a national matter, with which States can in no wise interfere. The jurisdiction of the Federal government absolutely excludes the States from directly or indirectly hampering or taxing commerce between the States.
>
> The claim of the State is also put upon the ground that the appellee can be compelled to pay a tax upon its gross earnings for the privilige of doing a local business in Indiana. This position is untenable. In no

event can a corporation, engaged in the business of interstate commerce, be taxed for the privilege of doing business in this, or any other, State. This principle early found a place in our jurisprudence. . . . Indeed, one of the great causes which led to the adoption of our Federal Constitution was the evil produced by the levying of tribute, in the form of taxes, upon the commerce between the States by some of the States under the Articles of Confederation. . . ."

State, ex rel. v. Woodruff Sleeping and Parlor Coach Co., 114 Ind. 155, 159.

The authority of the above decision of the state Supreme Court is fully recognized by the Department of Treasury in its administrative practice touching transportation and communication agencies. The statute nowhere makes any exception as to gross receipts received by such agencies from their business in interstate commerce. No distinction whatever is made between the taxability of gross receipts derived from the sale of goods in interstate commerce, and gross receipts derived from the service of carrying such goods to destination. The taxing officials, however, have in Regulation 140[8] exempted from the tax all gross receipts from services rendered in interstate commerce by any of the transportation or communication agencies. The selling and shipment of goods is commerce. If, as the Indiana officials have recognized, it is not lawful to lay a tax upon a mere instrumentality of interstate commerce, how can it be lawful *to lay a tax upon the commerce itself?*

[8].—"Reg. 140. The gross receipts derived by railroads, interurbans, pipe line, bus and truck lines from carrying charges of passengers, including Pullman service on sleeping and dining cars, freight and telephone or telegraph messages originating in the State of Indiana, the destination of which is outside of the State of Indiana on a continuous conveyance or which originated outside the State of Indiana and terminated therein, will not be included in gross income tax returns." (R. 121.)

The telegraph or telephone service used in negotiating sales, and the service of carrying the goods to their destination in other states and foreign countries, certainly have no sounder basis for exemption from the tax than have the proceeds derived from the sale and shipment of the goods themselves. The tax burden upon the latter is as direct as upon the former.

Clearly the Act makes no distinction. (Sec. 6(a) provides:

> "There shall be excepted from the gross income taxable under this Act: (a) So much of such gross income as is derived from business conducted in commerce between this state and other states of the United States, or between this state and foreign countries, to the extent to which the State of Indiana is prohibited from taxing under the constitution of the United States of America."

A statement of the principle controlling taxation of gross receipts, as developed by this Court in preceding decisions and many times since repeated in almost identical language, is found in the *Minnesota Rate Cases* as follows:

> "The principle which determines this classification underlies the doctrine that the states cannot, under any guise, impose direct burdens upon interstate commerce. For this is but to hold that the states are not permitted directly to regulate or restrain that which, from its nature, should be under control of the one authority, and be free from restriction, save as it is governed in the manner that the national legislature constitutionally ordains.
>
> Thus, the states cannot tax interstate commerce, either by laying the tax upon the business which constitutes such commerce, or the privilege of engaging in it, or *upon the receipts*,* as such, derived from it

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*Note.—All italics used in quotations in this brief are ours unless otherwise stated.

(citing many cases); or upon persons or property in transit in interstate commerce (citing cases)."

Simpson v. Shepard, 230 U. S. 352, 400.

A recent statement of the principle is as follows:

"... Persons have a constitutional right to engage in interstate commerce free from burdens imposed by a state tax upon the business which constitutes such commerce or the privilege of engaging in it or the receipts as such derived from it. *Minnesota Rate Cases (Simpson v. Shepard)* 230 U. S. 352, 400. Interstate commerce is not an abstraction; it connotes the transactions of those engaged in it and they enjoy the described immunity in their own right."

James v. Dravo Contracting Co., 82 L. Ed. advance paging 125, 138.

Definition of the Tax

In determining the Federal questions presented on this appeal, characterization of the tax is of no material consequence. Its name, definition, or any precise concept as to what it is laid upon, is unimportant. The sole question is whether the tax imposes a burden on interstate commerce that is not permitted by the Federal Constitution. This question can be answered only by reference to decisions of this Court and by the methods of construction traditionally used by it.[*]

However, it may throw light upon the weight to be given to the discussion of the court below to observe that it has had considerable difficulty in deciding to its satisfaction

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*.—*Crew Levick Co. v. Pennsylvania*, 245 U. S. 292, 294; *Macallen Co. v. Massachusetts*, 279 U. S. 620, 625; *Educational Films Corp. v. Ward*, 282 U. S. 379, 387; *Lawrence v. Tax Commission*, 286 U. S. 276, 280; *Gregg Dyeing Co. v. Query*, 286 U. S. 472, 476; *Senior v. Braden*, 295 U. S. 422, 429.

exactly what the nature of the tax is. In *Miles, et al. v. Department of Treasury* (opinion filed January 29, 1935), 193 N. E. 855, 861,[10] where the state Supreme Court first construed the tax, it said:

> "We conclude that the tax in question is an excise levied upon those domiciled in the State, upon the basis of the *privilege of domicile,* and that the burden may reasonably be measured by the amount of income."

On November 21, 1935, the state court filed an opinion "superseding former opinion," 209 Ind. 172, 188, in which the above language was expanded:

> "We conclude that the tax in question is an excise, levied upon those domiciled within the State or who derived income from sources within the State, upon the basis of the *privilege of domicile* or *the privilege of transacting business* within the State, and that the burden may reasonably be measured by the amount of income. The reasoning which justifies a tax upon the basis of domicile as readily supports and justifies a tax upon the basis of the right to receive income within, or transact business under the protection of the State."

And, in this case, 7 N. E. (2d) 944 (April 30, 1937), the court said:

> "The statute here under consideration levies a tax upon all who are domiciled within the State, based upon the *privilege of domicile,* and *transacting business,* and *receiving gross income,* within the State, and measured by the amount of gross income."

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[10].—The *Miles case* was appealed to this Court and dismissed on motion of the Attorney General on the ground that it was moot. (298 U. S. 640.) The record in the case will show, if it is complete, that the case was moot when the state Supreme Court decided it. A brief *amicus curiæ* was submitted to the state court showing its moot character and suggesting that it be dismissed by that court without decision.

The Attorney General argued in the state court and may argue here that a fourth privilege is taxed, namely, *the privilege of manufacturing,* "measured by the value of the goods manufactured" (R. 40-41).

The above definitions are of little value in determining the validity of the tax as applied to interstate commerce. The tax is not explained by calling it a tax on domicile, for it is also imposed upon foreign corporations and non-residents who receive income in the State or who receive income outside the State which is derived from sources within the State (Sec. 2, Ch. 50, Acts 1933; Reg. 2; R. 75). Neither is it explained by calling it a tax upon the privilege of transacting business, for, in many instances, it taxes where there is no business. Receipts received from any source whatever are taxed (Sec. 3 (f), Ch. 50, Acts 1933; Reg. 17; R. 78). The tax can logically be explained only *as a tax on gross receipts, which is exactly what the Act says it is, definitely and without ambiguity.* Further, examination of the Regulations under the Act reveals clearly that the administrative officers view it and apply it simply as a gross receipts tax.[11]

The Legislature made plain its intention to make gross receipts the subject of the tax by leaving out of the Act all language that would indicate that a privilege or occupation is taxed. The law from which the Act was copied, namely, the Mississippi Act of 1932, was plainly couched in the language of an occupation or privilege tax (as most

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[11].—Title of Act, "imposing a tax upon the receipt of gross income * * *"; Sec. 2, "levied *upon* the entire *gross income* * * *"; also, Sec. 3, (a)-(f); Sec. 6, (a)-(e); "excepted from the *gross income taxable* * * *"; Sec. 9, "not liable for a tax *upon his entire gross income";* Regulations, Art. 2, "The gross income tax act of 1933 *is primarily* and *in effect* a *gross receipts tax* * * *"; Reg. 16, "Tax shall apply to and shall be levied and collected *upon all gross income* * * *"; Reg. 21, *"Gross income* derived from sales *is taxable* * * *"; (Rec. 77-79).

other state excise taxes are), but all such language was carefully deleted by the Indiana Legislature.[12]

If the tax is an occupation tax, then as applied to appellant it is a tax upon the privilege of merchandising—the selling of its products. Gross receipts do not arise from manufacturing. They arise from the sale of the goods after the process of manufacture is complete. The receipts obtained—which are simply payment-money for the goods—include not alone the cost of manufacture, but also the direct and overhead costs of selling and usually the cost of shipment. The tax is directly related to the operation of selling and receiving money, as it is a tax upon the receipt of money. This is recognized by the state court in construing the statute on another point. Appellant contended below that as to all of its gross receipts, the tax should be computed at the rate of one-fourth of one per cent as a manufacturer, as stated in the Act, instead of at the rate of one per cent as a retailer. (Secs. 3 (a) and 3 (c), Ch. 50, Acts 1933; Reg. 47; R. 87). But the court held that the fact of manufacturing did not control the rate, that the character of the sale controlled it; and that when appellant sold, as would a wholesaler, to dealers or distributors for resale, the tax rate was one-fourth of one per cent, but when it sold, like a retailer, to an ultimate user or consumer, it must pay at the rate of one per cent; and said: "*The rate does not depend upon the business in*

[12].—Title of the Mississippi Act was: "An Act to provide for the raising of additional public revenue by imposing a tax upon the privilege of engaging in certain businesses in Mississippi, to provide for the ascertainment, assessment, etc." Ch. 119, Acts of Mississippi 1932. Title of the Indiana Act is: "An Act to provide for the raising of public revenue by imposing a tax upon the receipt of gross income, to provide for the ascertainment, assessment, etc." The Mississippi Act contained the word "privilege" twenty times and in each instance it was deleted in the Indiana law.

which the taxpayer is primarily engaged, but upon the activity from which each item of his gross income is received." (7 N. E. (2d) 941, 943; Statement as to Jurisdiction, p. 26; R. 46).

Thus, by the state court's holding, the tax is related to the activity of selling, and not to the activity of manufacturing. If the tax is an occupation tax at all, it is upon the occupation of selling merchandise, as in the *Crew Levick Case.* It is in fact neither. It is what the statute and the regulations call it—a tax upon gross receipts. And, "if the tax is what it calls itself, it is bad.'"[13] If it be deemed a tax upon the privilege of receiving gross receipts, the result is precisely the same. In either case, it is laid upon commerce itself, for selling is commerce and taking payment for things sold is commerce; and as to appellant's transactions in other states and foreign countries, it is a tax upon such commerce.

Whether the tax is laid directly upon gross receipts, or whether gross receipts are used merely as a convenient measure in computing the tax, as applied to gross receipts in interstate commerce the tax is invalid. Gross receipts cannot be a proper measure of any of the privileges included in the definition of the tax by the state court when considered in relation to interstate commerce. They cannot be a proper measure of the privilege of domicile, or of transacting business in interstate commerce, or of receiving dollars for goods sold in interstate commerce.

In *Galveston, H. & S. A. R. Co. v. Texas*, 210 U. S. 217, 227, the Court had before it a statute where gross receipts were the measure of the tax, and the Court said:

13.—*Meyer v. Wells, Fargo & Co.*, 223 U. S. 298, 300; also, *East Ohio Gas Co. v. Tax Commission*, 283 U. S. 465, 470.

"We are of opinion that the statute levying this tax *does amount to an attempt to regulate commerce among the states.* The distinction between a tax 'equal to' one per cent of gross receipts, and a tax of one per cent of the same, seems to us nothing, except where the former phrase is the index of an actual attempt to reach the property and to let the interstate traffic and the receipts from it alone. We find no such attempt or anything to qualify the plain inference from the statute, taken by itself. On the contrary, we rather infer from the judgment of the state court and from the argument on behalf of the state that another tax on the property of the railroad is upon a valuation of that property, taken as a going concern. This is *merely an effort to reach the gross receipts*, not even disguised by the name of an occupation tax, and in no way helped by the words 'equal to.'" (p. 227.)

So, whether the tax is laid upon the privilege of merchandising, as the state court apparently believes, or upon the privilege of receiving the proceeds of the merchandising, or upon the proceeds themselves, in any case, when applied to appellant's sales in interstate and foreign commerce, it is repugnant to Sections 8 and 10, Article I of the Federal Constitution.[14]

Nature of the Tax

The court below, in holding that the State may lawfully impose the tax upon gross receipts from interstate commerce, takes the position that the tax is general in form and application and does not in any way discriminate against interstate commerce, and in these respects differs from other state taxes on gross income which this Court has held invalid, including those considered in *Crew Levick*

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[14].—See cases cited on pages 10-11, *supra*.

Co. v. Pennsylvania, 245 U. S. 292, and the decisions preceding and following it.

In the first place, it is to be pointed out that the generality of such a tax in the sense used by the state court has never by this Court been considered a factor in determining whether it constitutes a direct and undue burden upon interstate commerce. The courts have always insisted that a tax must be general, that is, it must treat alike all within the class taxed; otherwise the tax is invalid by lack of due process of law or lack of equal protection of the law. This is a fundamental requirement in all taxes. But a tax may be entirely "general" in this respect and still be an illegal burden on interstate commerce, as both Federal and state courts have held in innumerable cases.

All through the opinion of the court below there is much stress laid on the term "general." Frequently it is used as practically synonymous with "universal," or as applying to every possible taxpayer in the State. In tax phraseology, the term "general" has never been given any such significance. It has not been considered that for a tax to be "general" it must be applicable to every possible taxpayer in the taxed area. In fact, there never has been such a tax. Even the ad valorem property tax has exceptions, and poll taxes, the most general type of all, are imposed only on persons between a minimum and maximum age.

Viewed in the light of the accepted meaning of the word "general" as used in tax terminology, the gross income tax of Indiana is not more general than other taxes which this Court has held to be invalid when applied to interstate and foreign commerce.

The gross income tax in question is *not* a general tax in the sense that it taxes every person or the entire gross in-

come of every person who receives gross income. Some of the more important exclusions, deductions and exemptions are the following:

There is the blanket exemption of all persons receiving less than One Thousand Dollars gross income per year. Among other exemptions are the following: Insurance companies which pay the State a tax of more than one per cent on premiums; non-profit labor organizations; non-profit agricultural organizations; non-profit horticultural societies; cemetery associations; fraternal societies operating for members; religious, charitable, scientific and fraternal organizations; business leagues; chamber of commerce groups; boards of trade; and civic leagues operated for benefit of social welfare. (Sec. 7.)* As to certain classes, gross *earnings* and *not* gross *receipts* are taxable. Among others, the following pay tax only upon their gross earnings and *not* their gross receipts: Banks, trust companies, building and loan associations, brokers, finance companies, dealers in commercial paper, and persons engaged in lending money or credit (Sec. 1 (g)). Also, domestic insurance carriers do not pay upon the portion of their income which becomes a reserve for the policy liability (Sec. 1 (h)). All persons are allowed certain deductions from gross income, including among others: Receipt of outright gifts (whether cash or property) (Reg. 70, R. 95), and pensions (Reg. 71, R. 96). Certain exclusions from gross income are allowed to all persons, including among others, the following: Receipts from insurance by reason of death of insured (Sec. 6 (d)); receipts from any insurance to amount of premiums paid (Sec. 6 (e));

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*Note.—Citations are to sections in Chap. 50, Acts 1933, found in the Appendix hereto, and to Regulations promulgated by Department of Treasury, Gross Income Tax Division, found in the Record.

salary from Federal Government or its agencies (Sec. 6 (a)); receipts from sale and interest on bonds of United States Government or its agencies (Sec. 6 (a)); receipts from maturities of Indiana municipal bonds (Reg. 62, R. 92); receipts from sales to United States Government or its agencies (Sec. 6 (c)); receipts on maturity of bonds or matured stock (Reg. 62, 103, R. 92, 111); money received as agent (Reg. 65, R. 93).

The reasonableness of these exemptions and exclusions is not here in question. The point is that *this tax is no more general,* in the sense of being universal in its application, *than other taxes which this Court has held to be unconstitutional burdens on interstate commerce.*

The case of *Crew Levick Co. v. Pennsylvania,* supra, which is closely analogous to the instant case, provides a fair example. In that case foreign commerce was involved just as in this case, and both Sections 8 and 10 of Article I of the United States Constitution were before the Court as in this case.

The *Crew Levick Case* (245 U. S. 292, note) arose on a Pennsylvania statute which provided:

> "That . . . each retail vendor of or retail dealer in goods, wares and merchandise shall pay an annual mercantile license tax of $2, and all persons so engaged shall pay one mill additional on each dollar of the whole volume, gross, or business transacted annually. Each wholesale vendor of or wholesale dealer in goods, wares and merchandise shall pay an annual mercantile license tax of $3, and all persons so engaged shall pay one-half mill additional on each dollar of the whole volume, gross, of business transacted annually."

Manifestly this tax was general to an unusual degree. The subject of the tax was the activity of retailing or

wholesaling goods, wares and merchandise of every sort and kind. .There were no exemptions or exclusions. It applied from the lowest to the highest. It taxed all alike, from the peanut vendor on the street to the manufacturer with an investment of millions. And there was no discrimination in the tax. It applied to all dealings in all kinds of goods, wares and merchandise, whether such dealings were local and intrastate or whether they were interstate and foreign. So the fact is that the Pennsylvania tax held invalid by this Court in the *Crew Levick Case,* was at least as general in its application as the gross income tax of Indiana now under consideration.

Concerning this general and non-discriminatory tax of Pennsylvania, this Court said:

> "The tax now under consideration, so far as it is challenged, fully responds to these tests. It bears no semblance of a property tax, or a franchise tax in the proper sense; nor is it an occupation tax except as it is imposed upon the very carrying on of the business of exporting merchandise. It operates to lay *a direct burden* upon every transaction in commerce *by withholding,* for the use of the State, a *part of every dollar received in such transactions.* That it applies to internal as well as to foreign commerce cannot save it; for, as was said in *State Freight Tax Case,* 15 Wall. 232, 277, 21 L. ed. 146, 162: 'The State may tax its internal commerce, but if an Act to tax interstate or foreign commerce is unconstitutional, *it is not cured by including in its provisions subjects within the domain of the state.'* That portion of the tax which is measured by the receipts from foreign commerce necessarily varies in proportion to the volume of that commerce, and hence is a direct burden upon it."
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> *Crew Levick Co. v. Pennsylvania,* 245 U. S. 292, 297-298.

The occupation tax considered by this Court in *Fisher's Blend Station* and *Puget Sound Stevedoring Co. Cases, supra,* was also a general tax. Instances of taxes of broad and non-discriminatory application to gross receipts are to be found in many other states where they are not enforced against receipts from interstate commerce because of the recognized illegality thereof under the Federal commerce clause. See p. 40, *infra,* and note.

Any tax which directly burdens interstate commerce is invalid regardless of whether it discriminates against or in favor of such commerce. This Court, in many instances where the tax was non-discriminatory and of general application within the class chosen for taxation, has held a state tax to be invalid as applied to interstate and foreign commerce.

> "The state may tax its internal commerce; but if an act to tax interstate or foreign commerce is unconstitutional, *it is not cured* by including in its provisions subjects within the domain of the state."
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> *Phila. & Reading R. Co. v. Pennsylvania,* 82 U. S. (15 Wall.) 232, 277.

> "It is strongly urged, as if it were a material point in the case, that no discrimination is made between the domestic and foreign drummers—those of Tennessee and those of other states; that all are taxed alike. *But that does not meet the difficulty.* Interstate commerce cannot be taxed at all, even though the same amount of tax should be laid on domestic commerce, or that which is carried on solely within the state."
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> *Robbins v. Taxing District,* 120 U. S. 489, 497.

After referring to the decision and the language above quoted, this Court in the following case said:

> "This last observation meets the argument that might be made in the present case; namely, that the law is general in its terms, and taxes receipts for all trans-

portation alike, *making no discrimination* against receipts for interstate or foreign transportation, and hence cannot be regarded as a special tax on the latter. The decision in the case cited shows that this does not relieve the tax from its objectionable character.

Phila. & S. M. S. S. Co. v. Pennsylvania, 122 U. S. 326, 340.

"The tax affects the *whole business without discrimination.* There are sufficient modes in which the internal business, if not already taxed in some other way, may be subjected to taxation, without the imposition of a tax which covers the entire operations of the Company."

Leloup v. Port of Mobile, 127 U. S. 640, 647.

"Of course, it does not matter that the plaintiffs in error are domestic corporations, or *that the tax embraces indiscriminately gross receipts from commerce within as well as outside of the State.*"

Galveston, H. & S. A. R. Co. v. Texas, 210 U. S. 217, 228.

"The fact that the law under which the tax was imposed was a *general* law, *touching all sales of the class,* and not aimed specially at exports, would not help the defendant if, in this case, the tax was 'laid on articles exported from any state,' because that is forbidden in terms by the Constitution."

A. G. Spalding & Bros. v. Edwards, 262 U. S. 66, 69.

"So, too, a tax upon the gross receipts from interstate transportation or transmission, *whether receipts from intrastate transportation or transmission are equally taxed or not,* is an unlawful tax because a direct burden upon interstate commerce."

Sonneborn Bros. v. Keeling, 262 U. S. 506, 515.

"*The fact that a portion of a business is intrastate and therefore taxable does not justify a tax either*

upon the interstate business or upon the whole business without discrimination . . . There are 'sufficient modes' in which the local business may be taxed without the imposition of a tax 'which covers the entire operations.' (Citing cases) *Where the tax is exacted from one doing both an interstate and intrastate business, it must appear that it is imposed solely on account of the latter; that the amount exacted is not increased because of the interstate business done; that one engaged exclusively in interstate commerce would not be subject to the tax;* . . ."

Cooney v. Mountain States Tel. & Tel. Co., 294 U. S. 384, 392-393.

The court below suggests that the tax on manufacturers and wholesalers seems to discriminate in their favor. This is on the assumption that the greater part of all goods sold in interstate commerce is to distributors or dealers for resale and therefore are taxed at the lower rate. This assumption is unsound. It is well known that much the larger part of capital goods is sold to ultimate users and consumers, and that a substantial part of consumers goods is so sold. Gross receipts from such sales are taxed at the higher rate of one per cent.

But in any case, whether manufacturers pay chiefly at the higher or the lower rate can have no bearing on the legality of the tax. The difference is wholly adventitious. It does not rest upon the character of the tax; and if a difference in rate is to make the distinction between a legal and an illegal burden, the problem then will be as to how great a difference in rate will be necessary in order to make one tax valid and another invalid. It is obvious that the legality of a burden on interstate commerce can not depend upon the size of that burden. Once the validity of such a tax is recognized, the courts can place no limit upon

the amount, and legislatures will be free to impose a tax upon gross receipts from interstate commerce that may destroy the commerce.

> "Once the lawfulness of the method of levying the tax is affirmed, the judicial function ceases. He deludes himself by a false hope who supposes that if this court shall at some future time conclude the burden of the exaction has become inordinately oppressive, it can interdict the tax."
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> *Stewart Dry Goods Co. v. Lewis*, 294 U. S. 550, 563.

It is clear on reason that a state tax that directly regulates, restricts or burdens commercial transactions in interstate commerce cannot be relieved of its constitutional infirmity because it is applied in the same manner to like transactions within the borders of the state. The instant case well illustrates this principle.

The effect of the tax in question is not remote or indirect. It is immediate and direct. It takes hold of every dollar that results from commerce and extracts from it a percentage toll. Not a dollar from any mercantile transaction escapes it. This tribute the State with perfect right may exact from its domestic transactions: That is within its sole jurisdiction, but taxation of interstate commerce is not within its jurisdiction. The Constitution does not say that the power of Congress to regulate commerce with foreign nations and among the several states shall exist only where a state fails to exercise its own power to regulate commerce within its borders. There is no indication in the commerce clause that its authority over interstate and foreign commerce should be limited by anything the state might do with respect to its own commerce. There is no power reserved to the state to tax interstate commerce,

and there is no restriction on Congress as to regulation of commerce that is interstate.

So, the fact that the state sees fit to exercise its taxing functions as to commercial transactions within its borders, or as to the receipts derived from such transactions, does not in any way create for it an authority to do the same thing as to transactions within the realm of interstate commerce. Taxing the privilege of engaging in domestic commerce cannot give rise to an authority it otherwise did not have to tax the privilege of engaging in interstate commerce. The generality of the tax imposed by the State cannot take off the constitutional limitations on the power of the State. Thus, it is not necessary that regulation be directed at interstate commerce alone, or discriminate against interstate commerce, in order to come within the inhibition of the Constitution. The commerce clause says nothing of that sort, and the imposition of a burdensome tax upon all commerce does not lessen its objectionableness as to the type of commerce protected by such clause. This, we think, is the conclusion that must be drawn from the many decisions of this Court upon the subject.

The burdensome effect which this gross receipts tax will have upon interstate commerce is further illustrated by the system of taxation now developing. Many states now have "use" or "compensating" taxes which are levied upon the use of goods within the state. They are complementary to existing sales taxes that now are applied only to intrastate sales. The use tax is always levied at the same rate and is equal in amount to the sales tax. The use tax laws permit the amount of any sales tax *paid within the state* to

be credited against the use tax.[15] This cancels the use tax where the sales tax is paid within the state. Except in few instances, credit is not allowed for any sales or other excise tax collected by another state. Obviously, where the use tax is established, the interstate seller must either pay the tax himself or increase his price to allow for the use tax payable in the state to which the goods are shipped.[16]

If a gross receipts tax, as here in question, or a sales tax, be laid upon the seller in the state of origin, the practical result is that a burden will fall doubly upon interstate sales, and singly upon intrastate sales. For example: assume appellant has a competitor in the State of Ohio, manufacturing the same line of products. Ohio has in force a three per cent use tax. Appellant's products sold in the State of Ohio must there submit to the use tax. Its Ohio competitor pays only the three per cent sales tax, which is credited against the use tax. If appellant in addition to paying the

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[15].—Laws of Alabama 1936, Act 126, Sec. 2(d), 2% tax; Laws of Arkansas 1937, Act 154, Sec. 4 (F), 2% tax; Laws of California, Deering's Supp. 1935, Sec. 4(a), p. 2020, 3% tax; Laws of Colorado 1936, Chapter 11, Sec. 2(a), 2% tax; Laws of Iowa 1937, S. F. No. 317, Sec. 3(1), 2% tax; Local Laws New York City 1937, No. 21, Sec. 2(c), 2% tax; Laws of Ohio, General Code, Sec. 5546-26(1), 3% tax; Laws of Wyoming 1937, Chapter 118, Sec. 4 (a), 2% tax. *Cf. Henneford v. Silas Mason Co.*, 300 U. S. 577, 587.

The laws of the following States still contain an exemption from the use tax where a sales tax has been paid in the State or ***in any other State***:

Laws of Kansas 1937, H. B. No. 619, Sec. 5, 2% tax; Laws of Michigan 1937, H. B. 317, Sec. 4(f); Laws of Oklahoma 1937, H. B. 589, Sec. 5(c), 2% tax; Laws of Utah 1937, Ch. 114, Sec. 4(d), 2% tax.

[16].—Some of the use statutes provide that the seller shall collect the tax. Laws of California, Deering's Supp. 1935, Sec. 6, p. 2021; Laws of Iowa 1937, S. F. 317, Sec. 5(2); Laws of Michigan 1937, Act 94, Sec. 5; Laws of Ohio, General Code, Sec. 5546-28 (Jan. 1938 Supp.); Laws of Utah 1937, Ch. 114, Sec. 6; Laws of Wyoming 1937, Ch. 118, Sec. 6.

three per cent use tax in Ohio (or increasing its price three per cent, or collecting from the purchaser) is compelled to pay a gross receipts tax of one per cent in the State of Indiana, it is plain that such sales in interstate commerce must bear a burden of one per cent which the competitor doing intrastate business in Ohio does not bear. Free intercourse between the states will be seriously impeded if a tax on gross receipts can be applied in the state of origin and a use tax applied in the state of destination. With the rapid spread of the sales tax and its complement the use tax as a method of raising revenue, it is safe to say that soon the use tax in the state of destination in conjunction with a gross receipts tax or a sales tax in the state of origin would impose a double burden on interstate commerce which intrastate commerce would not bear.

The Tax is Not in Lieu of Property Taxes

The court below implies that the gross income tax is in lieu of other taxes and therefore can be sustained upon the theory that a tax "*in lieu of property taxes,*" if reasonable in amount, may be measured by gross receipts. This argument must fall with the premise on which it is based. The gross income tax is not in lieu of property taxes. Appellant (R. 25) and all other taxpayers continue to pay the regular property taxes, and the assessed valuation of their property for such purpose is established in the usual manner. The tax may in some counties reduce property taxes, in others, not; but all state excises imposed for revenue are intended to, and actually do, relieve and reduce property taxes to some extent. The "in lieu" tax theory relates only to taxes which are substitutes for property taxes.[17] This Court has held that a state in taxing property (usually

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[17].—*Leloup v. Port of Mobile*, 127 U. S. 640, 645, 646; *Galveston, H. & S. A. R. Co. v. Texas*, 210 U. S. 217, 226-227.

of a foreign corporation that is a carrier) within its boundaries is not limited to the mere cash value of the tangible property, but may determine the value of such property on the basis that it is part of a going concern transacting interstate as well as intrastate business; but the foundation of all such taxes is that the tax levied *is in lieu of all other property taxes.* The state court, in its opinion in this case, endeavors to extend the "in lieu" theory by a statement that consideration must be given to other acts passed at the same session of the Legislature. This Court has had before it like situations where the same question was raised. In the case of *Meyer v. Wells, Fargo & Co., supra,* pp. 300-301, the Court said:

> "*It was argued in some detail that taking into account the rest of the act and other statutes passed later at the same session, this really was a property tax.* But the scope and purport of the act, so far as it affects express companies, are too obvious to admit such a view. *The tax is in addition to the taxes levied and collected upon an ad valorem basis . . .*"[18]

The distinction is also emphasized by writers of recognized standing. The reputed author of the Indiana Gross Income Tax Act himself has said:

> " . . . there is now no doubt of the invalidity of a state tax upon gross income derived from foreign or interstate commerce (*Meyer v. Wells, Fargo & Co.,* 223 U. S. 298 (1912); *Crew Levick Co. v. Pennsylvania,* 245 U. S. 292 (1917); *Galveston, etc., Ry. v. Davidson,* 93 S. W. 436 (Tex. Civ. App. 1906); *State Tax on Gross Receipts,* 15 Wall. 284 (U. S. 1872) must be deemed to be overruled, so far as it decides to the contrary),

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[18].—See, also, *United States Express Co. v. Minnesota,* 223 U. S. 335, 346, 347-348; *Cudahy Packing Co. v. Minnesota,* 246 U. S. 450, 454, 456.

although a state gross income tax limited to income from intra-state commerce clearly is not an offender. *Ohio Tax Cases,* 232 U. S. 576 (1914). *The only exception to this rule of invalidity is in the situation where a gross income tax is laid in lieu of one upon the property of a carrier; in such case the impost is essentially a property tax. Postal Tel. Co. v. Adams,* 155 U. S. 688 (1895); *State v. United States Express Co.,* 114 Minn. 346, 131 N. W. 489 (1911), aff'd; 223 U. S. 335 (1912). Even a tax upon gross earnings from interstate or foreign commerce seems also to be unconstitutional. *State v. Wells, Fargo & Co.,* 146 Minn. 444, 179 N. W. 221 (1920). See also *McHenry v. Alford,* 168 U. S. 651 (1898)."

Robert C. Brown, Constitutional Limitations on Progressive Taxation of Gross Income (1937, Iowa Law Review, Volume 22, pages 250-251).

Another writer has said:

"There is no dispute that gross receipts from interstate commerce are not taxable directly as such."

"The Court is satisfied when the state shows that the income is taken as a fair measure of the value of the property assessed for taxation, or *when a tax on income is in substitution for a property tax.*"

Indirect Encroachment on ~~Federal~~ Authority by Taxing Power of the State. Thomas Reed Powell, 32 Harvard Law Review, 377, 398.

In view of the state court's holding that the gross income tax is an excise tax, not a property tax (*Miles v. Department of Treasury,* 209 Ind. 172, 188), and the fact that the tax is levied in addition to all other taxes of every character, there is left no ground for the contention that the tax is in lieu of property taxes.

Cases Cited by the State Court

The case chiefly relied upon by the state court is *American Manufacturing Co. v. St. Louis,* 250 U. S. 459. This Court there held valid a license tax upon manufacturing measured by the value of the goods manufactured. In that case, the Court was careful to point out that the tax was payable only as to products actually manufactured in St. Louis and that the tax was measured by the value of the goods manufactured regardless of where sold. The Court said:

> "No tax has been or is to be imposed upon any sales of goods by plaintiff in error *except goods manufactured by it in St. Louis* under a license conditioned for the payment of a tax upon the amount of the sales when the goods should come to be sold." (250 U. S. 463.)

This Court, in stating the facts of the case, also said that the amount of the tax "is ascertained by and proportioned to the amount of sales of the manufactured goods whether sold within or without the State, and whether in domestic or interstate commerce." (250 U. S. 460.)

The theory of the *American Manufacturing Case* cannot be applied to the tax here for three reasons: (1) the tax is not laid on the privilege of manufacturing; (2) the tax, even if it were on the privilege of manufacturing, is not measured by the value of *all* goods manufactured; and (3) the tax is not limited to the value of the goods manufactured.

The discussion on the character of the tax at pages 16-19, above, relates to the first distinction and is not repeated here. The tax is not levied upon the privilege of manufacturing, and the state court has never stated that it is levied upon such privilege. It must be noted that the tax is upon the "entire" gross receipts of appellant. The

tax applies to appellant's receipts from investments, from the sale of goods other than its own products which it may purchase and resell, and to receipts from any source whatsoever. The tax is expressly stated by the statute and the Regulations under which it is administered to be "upon gross receipts," and in the case of appellant and others in like situation, it is a tax upon gross receipts from sales to customers located in other states and in foreign countries, and hence is a tax either upon the privilege of engaging in interstate and foreign commerce or upon the privilege of receiving payment for goods sold in interstate and foreign commerce.

As to both first and second distinctions, *supra,* the tax in this case, unlike the tax in *American Manufacturing Co. Case,* is not imposed upon the value of *all* goods manufactured in the State, nor upon gross receipts from the sale of *all* goods manufactured in the State. Under Regulation 191 (R. 143), promulgated July 31, 1934, the taxpayer was given the right to defer the reporting of receipts derived from activities carried on at a business situs outside the State of Indiana. By Regulation 193 (4) (R. 146), promulgated December 31, 1935, which revoked Regulation 191, such receipts of the taxpayer were designated as non-taxable receipts. (Cf. Sec. 2, Ch. 50, Acts 1933, which provides for the imposition of the tax upon both residents and non-residents who *derive income from sources within the State.*) In 1937 the legislature carried Regulation 193 (4) into the amended Act. Sec. 1(m), Ch. 117, Acts 1937 (see Appendix B), contains the provision that with respect to Indiana corporations "gross income" shall not include gross receipts from a business situated and regularly carried on at a legal situs outside of the State.

So, under Regulation 193 (4) and Section 1(m) of the 1937 law, manufacturer Y making products within the State may

ship them to warehouse or branch stores outside the State, and from such points sell the products without paying the Indiana tax upon the receipts. And this is true even though the purchaser sends his payment directly to Y's home office in Indiana, or though the cash, check or draft for the goods on being received at the branch or warehouse outside of the State is forwarded to the home office of Y in Indiana. But manufacturer Z who produces his products in the State of Indiana and ships them from Indiana directly to purchasers in other states and foreign countries is taxed upon all of the receipts from such sales under the state court's construction. Now if manufacturer Z should change his mode of business to that of manufacturer Y by selling his products from a situs in other states, he would be free from the Indiana tax on such receipts. In other words, a manufacturer by going out of interstate commerce originating in Indiana and into commerce originating in some other state escapes the burden of the tax. *Yet he may continue to enjoy and exercise within the State the privilege of manufacturing his goods there and of actually receiving his gross income in Indiana.* The only difference between Y and Z is that Y ships to himself in another state and then sells from that situs, while Z sells and ships directly from the home office and plant to the customer in another state.

The *American Manufacturing Co.* decision is based on the proposition that a state may tax the *local privilege of manufacturing* and measure that tax by the value of the goods manufactured, whether sold "*within or without the State,*" or in domestic or interstate commerce. (250 U. S. 463.) Under the instant law, a manufacturer producing all of his products in Indiana, pays a tax only upon receipts from sales made (a) in interstate commerce from Indiana, or (b) within the State of Indiana. No tax is levied on

receipts from sales made from a situs "without the State," though the goods are manufactured in Indiana.

Thus the tax in question clearly is not (1) a tax *on the privilege of manufacturing,* nor (2) a tax *measured by the value of all goods manufactured,* as in the *American Manufacturing Co. Case.*

As to distinction (3) mentioned *supra,* the tax is not limited to the value of the goods *in Indiana.* The Act in Section 1 (f) allows deduction of "freight prepaid by the taxpayer and repaid to him by the purchaser" which is the only provision which in any way permits deduction of transportation costs. This exemption has been strictly limited by Regulation 67, which provides in part:

> "In order to claim deductions of this kind on gross income tax returns, the shipper must have actually prepaid freight for the purchaser. In no case can the freight charges be deducted as an expense by either the shipper or his customers, and this deduction can in no way refer to freight charges which are a cost of doing business." (R. 93.)

In every case, therefore, where the goods are sold at a delivered price and delivery is made by train, truck, express or parcel post, the tax falls upon the entire gross receipts and not on the value of the goods in Indiana. Of course, in some situations the freight charge is a very substantial portion of the total selling price, and the tax in question therefore bears directly upon the selling price of the goods in interstate commerce and not upon their value in the State of Indiana. There is thus a tax charge upon the cost of interstate carriage. The suggestion of the state court that the effect of this tax might be avoided by changing the method of doing business is not an answer. The taxpayer is not required to change his method of doing

business to meet a taxing statute. "Surely he can not be compelled to take this inconvenient and expensive course." *Stockard v. Morgan*, 185 U. S. 27, 32.

The tax in the *American Manufacturing Co. Case* was limited to the value of the goods in St. Louis. The necessity of such a limitation was recognized in *Hope Natural Gas v. Hall*, which later was affirmed by this court. In fact, the state court in the last mentioned case specifically so limited the scope of the tax:

> "Consequently, we are *warranted in presuming that the Legislature did not mean to include, as an element of value, so much of the gross proceeds of the sale of an article in interstate commerce as is represented by the cost of transportation, and we restrain the operation of the statute accordingly. This presumption* and this limitation *are strengthened by the concluding sentence of the statute, whereby the measure of the tax is declared to be the value of the product in this state,* regardless of place of sale or delivery outside of state. If the sale of a commodity produced in this state imposes on the seller delivery in another state, then the sale price necessarily includes the cost of the delivery. Such sale price would not reflect the worth of the commodity in the state, but the worth within the state plus the cost of transportation. If the taxation value of the products named in the statute be limited to their value in the state, and before they enter interstate commerce, the statute does not manifest a purpose to violate article 1 of the federal Constitution, and we so hold."
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> *Hope Natural Gas Co. v. Hall*, 102 W. Va. 272, affirmed 274 U. S. 284.

Thus, for all three reasons set forth *supra*, the *American Manufacturing Case* fails to support the gross income tax.

Other cases cited or discussed in the state court's opinion are not in point for the following reasons:

Peck & Co. v. Lowe, 247 U. S. 165, involved the Federal net income tax and the commerce clause was not in question. *Bass, Ratcliff & Gretton, Ltd. v. Tax Commission*, 266 U. S. 271, and *Shaffer v. Carter*, 252 U. S. 37, involved net income taxes. *Cudahy Packing Co. v. Minnesota*, 246 U. S. 450, and *Pullman Co. v. Richardson*, 261 U. S. 330, involved taxes, measured by gross earnings or gross receipts, in lieu of other property taxes. *Postal Telegraph-Cable Co. v. Richmond*, 249 U. S. 252, involved a license or occupation tax restricted to intrastate business, and the tax was assailed "upon inadequate evidence and upon purely empirical calculations which we are asked to adopt." (pp. 257, 261.)

It is unnecessary here to discuss the remaining cases referred to by the state court, as they all directly support appellant's contention and are elsewhere cited in this brief. In its discussion of the *Crew Levick Co.* and *American Manufacturing Co.* cases, the court below intimates that the former was virtually overruled by the latter. This can hardly be true. The latter case was decided at the succeeding term by the same Justices, and the opinion written by the same Justice as the former case. In *United States Glue Co. v. Oak Creek, supra,* decided at the same term as *Crew Levick Co. Case,* the latter was expressly reaffirmed and used as a basis for the distinction between a net income tax and a gross income tax as applied to the commerce clause; and on this distinction, the *United States Glue Co. Case* has been the controlling decision to the present time, and the *Crew Levick Co. Case* has been constantly cited with it by this Court. Further, in the *American Manufacturing Co. Case* opinion, the Court distinguishes the case from the *Crew Levick Case* and clearly indicates its continued approval of the latter. Also, and more important, it is to be noted that

the Court has had occasion to refer to the *American Manufacturing Co. Case* but relatively few times, and then often to distinguish the then pending case with the effect of limiting the scope of the *American Manufacturing Case*;[19] on the other hand, the *Crew Levick Co. Case* has been cited in the reports of this Court at least twenty-four times, and in each instance it has been referred to with other decisions as controlling in the case then before the Court, or cited, sometimes in dissenting opinions, as one of the authorities on the rule that a tax on gross receipts derived from interstate commerce is invalid.[20]

19.—*Shaffer v. Carter* (1920), 252 U. S. 37; *Public Utilities Commission of Rhode Island v. Attleboro Steam and Electric Company* (1927), 273 U. S. 83; *Hope Natural Gas Co. v. Hall* (1927), 274 U. S. 284; *Indian Motocycle Co. v. United States* (1931), 283 U. S. 570; *Utah Power and Light Company v. Pfost* (1932), 286 U. S. 165; *Federal Compress and Warehouse Co. v. McLean* (1934), 291 U. S. 17; *Liggett & Myers Tobacco Co. v. United States* (1937), 299 U. S. 383, 387.

20.—*United States Glue Co. v. Oak Creek* (1918), 247 U. S. 321; *Standard Oil Co. v. Graves* (1919), 249 U. S. 389; *Corn Products Refining Co. v. Eddy* (1919), 249 U. S. 427; *American Manufacturing Co. v. St. Louis* (1919), 250 U. S. 459; *Shaffer v. Carter* (1920), 252 U. S. 37; *Spalding & Bros. v. Edwards* (1923), 262 U. S. 66; *Sonneborn Bros. v. Keeling* (1923), 262 U. S. 506; *Texas Transport & Terminal Co. v. City of New Orleans* (1924), 264 U. S. 150; *Ozark Pipe Line Corp. v. Monier* (1925), 266 U. S. 555; *Jaybird Mining Co. v. Weir* (1926), 271 U. S. 609; *Di Santo v. Pennsylvania* (1927), 273 U. S. 34; *Northwestern Mutual Life Ins. Co. v. Wisconsin* (1927), 275 U. S. 136; *Macallen v. Massachusetts* (1929), 279 U. S. 620; *New Jersey Bell Tel. Co. v. State Board of Tax and Assessment* (1930), 280 U. S. 338; *Burnet v. Coronado Oil & Gas Co.* (1932), 285 U. S. 393; *Fox Film Corp. v. Doyal* (1932), 286 U. S. 123; *Anglo-Chilean Nitrate Sales Corp. v. Alabama* (1933), 288 U. S. 218; *Nashville, etc., R. Co. v. Wallace* (1933), 288 U. S. 249; *Virginia v. Imperial Coal Sales Co.* (1934), 293 U. S. 15; *Stewart Dry Goods Co. v. Lewis* (1935), 294 U. S. 550; *Fisher's Blend Station v. Tax Commission of Washington* (1936), 297 U. S. 650; *Henneford v. Silas Mason Co.* (1937), 300 U. S. 577; *Puget Sound Stevedoring Co. v. Tax Commission*, 82 L. ed. advance paging 64; *James v. Dravo Contracting Co.*, 82 L. ed. advance paging 138.

Attitude of Other States on Gross Receipts Tax

It is significant that of the several states which have passed sales, gross income, occupation or other excise tax laws by which in any manner gross receipts are made the measure of the tax, approximately four-fifths by their own volition have recognized that they may not impose a tax upon or measured by gross receipts derived from interstate commerce without violation of Article I, Sections 8 and 10 of the Federal Constitution. This deference to the commerce clause is by terms of the legislation, by administrative regulations, by opinion of attorney general, or by state court decision, as indicated in the footnote.[21]

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[21].—In a majority of the jurisdictions referred to in this note, the statute includes a provision identical with or closely analogous to Section 6 in the Indiana Gross Income Tax Act of 1933. **Alabama**—No. 194, Laws of Alabama, 1935, as construed by opinion of Attorney General, May 15, 1937, (Sales Tax); **California**—Laws of California, Deering Sup. 1935, Act 8493, as construed by Ruling 26, (Sales Tax); **Colorado**—Ch. 230, Laws of Colorado, 1937, as construed by Regulation 14, (Sales Tax); **Georgia**—*American Mills Co. v. Doyal* (1933), 46 Ga. App. 236, (Sales Tax); **Illinois**—Cl. 196, Laws of Illinois, 1933, p. 924, as construed by Article 5 of Rules and Regulations, (Occupation—Sales Tax); **Iowa**—Ch. 82, Laws of Iowa, 1933, first Special Session reenacted by Cl. 191, Laws of Iowa, 1937, as construed by opinion of Attorney General, April 6, 1934, (Sales Tax); **Kansas**—S. B. 522, Laws of Kansas, 1937; and see Rule 2, (Sales Tax); **Louisiana**—Act No. 75, Laws of Louisiana, 1936, as construed by opinion of Attorney General, August 29, 1936; *State v. Albert Mackie Co., Ltd.* (1918), 144 La. 339, (Sales Tax); **Michigan**—Public Act No. 167, Laws of Michigan, 1933, as construed by Article 31 of Rules and Regulations, and by *J. B. Simpson, Inc. v. O'Hara, et al.* (1936), 277 Mich. 55, (Sales Tax); **Mississippi**—Ch. 119, Laws of Mississippi, 1934, as construed by opinions of Attorney General, March 1, 1933 and December 18, 1934, (Privilege—Sales Tax); **Missouri**—Laws of Missouri, 1937, p. 552, as construed by Ch. III (a) of Rules and Regulations, and by opinion of Attorney General, November 19, 1935, (Sales Tax); **New Mexico**—Sec. 202, Ch.

73, Laws of New Mexico, 1935, as amended by H. B. 151, Laws of 1937, as construed by opinion of Attorney General, October 22, 1937, (Occupation—Gross Income Tax); **New York City**—(1) Local Law 22, Laws of New York City, 1937, as construed by Regulations, Article 37, and *National Cash Register Co. v. Taylor, Comptroller* (Nov. 23, 1937, New York), 11 N. E. (2d) 881. (Gross Receipts Tax) (2) Local Law 20, Laws of New York City, 1937, as construed by Regulations, Article 94, and *National Cash Register Co. v. Taylor, Comptroller, supra,* (Sales Tax); **North Dakota**—S. B. 80, Sec. 2, Laws of North Dakota, 1937, as construed by Rule 56, (Sales Tax); **Ohio**—Sec. 5546-2 of General Code of Ohio, as construed by Regulations, Article VIII-K, (Sales Tax); **South Dakota**—Ch. 205, Laws of South Dakota, 1935, as construed by Regulations, Article 6, and opinion of Attorney General, June 26, 1937; *State ex rel. v. Welsh* (1933), 61 S. D. 593, (Occupation—Sales Tax); **Texas**—Ch. 2, Article 7058-7064, Texas Civil Statutes, as construed by opinions of Attorney General, July 22, 1936, November 16, 1936, and February 2, 1937, (Occupation Tax); **Utah**—Ch. 63, Laws of Utah, 1933, as construed by Par. 6, Revised Regulations of January 1, 1936, (Sales Tax); **Washington**—Ch. 180, Laws of Washington, 1935, as amended by Cl. 227 (1937); (1) Title II, as construed by Rule 198. "The state Supreme Court recognized that state taxation of gross income derived from interstate commerce is forbidden by the Commerce Clause"—*Fisher's Blend Station v. Tax Commission,* 297 U. S. 650, at 652. (Occupation—Gross Income Tax). (2) Title III, as construed by Rule 198. (Sales Tax). (3) Title V, as construed by Rule 198, (Public Utilities—Gross Operating Revenue Tax); **West Virginia**—Article 13, West Virginia Code of 1937, as construed by Bulletin of May 12, 1934, and opinion of Attorney General, August 10, 1934; *Hope Natural Gas Co. v. Hall* (1926), 102 W. Va. 272, (Occupation Tax).

II

The Tax is Invalid as Applied to the Interest from Tax Exempt Bonds

The second error assigned is based upon the ground that the Gross Income Tax Act, as applied to interest from "tax exempt" bonds of Indiana municipalities, is an impairment of contract under Article 1, Section 10, of the Constitution of the United States.

In the trial court, it was stipulated that the bonds of Indiana municipal corporations issued prior to the effective date of the Gross Income Tax Act and held by appellant, "by the statutes of Indiana in force now and at the time of the issuance of such bonds . . . are declared to be exempt from taxation" (R. 29). The trial court found the bonds to be exempt from taxation, and the imposition of the tax on the interest from such bonds was held to be an impairment of contract contrary to the Constitution of the United States (R. 18), and held the Act unconstitutional in so far as it required the levy of the gross income tax upon the interest from such bonds (R. 20). On appeal to the Supreme Court of Indiana, the appellees in their brief assumed the existence of a contract of exemption from taxation, and limited their argument to the scope of the contract (R. 38-40). The State Supreme Court in its opinion conceded the existence of the contract. It stated:

> "The bonds from which the income was received are specifically exempted from taxation . . ." (R. 46).

So this inquiry may properly begin with the assumption that a contract exempting the bonds from taxation existed between the appellant and the various municipalities.

> *Hale v. Iowa State Board of Assessment and Review,* 82 L. Ed., advance paging, 66, 68;
>
> *Storen v. J. D. Adams Manufacturing Company,* 7 N. E. (2d) 941, 943.

The provisions of the law existing at the time of the issuance of a bond specifically exempting it from taxation become a part of the contract of the bondholder, and not

subject to impairment by the State.[22] This Court, however, need not decide this point, since the existence of a contract is conceded.

The Court Must Determine the Scope of the Contract

The power resides with this Court, when impairment of contract is urged, to determine the effect and meaning of the contract.

> *Hale v. Iowa State Board of Assessment and Review,* 82 L. Ed., advance paging, 66, 68;
> *State ex rel. Anderson v. Brand,* 82 L. Ed., advance paging, 444, 448;
> *United States Mortgage Co. v. Matthews,* 293 U. S. 232, 236;
> *Funkhouser v. Preston,* 290 U. S. 163, 167.

The state court's declaration that the exemption does not apply to any excise tax upon a privilege, and that the gross income tax is of that type, is therefore the very inquiry to be made in this case. The original statute providing for the exemption of municipal obligations from taxation was adopted in 1903 as a *separate and independent* Act. Cf. *Hale v. Iowa State Board of Assessment and Review,* 82 L. Ed., advance paging, 66, 69. In its entirety, the Act reads as follows:

> "AN ACT to exempt from taxation all bonds, notes and other evidences of interest-bearing debt issued by the State or by municipal corporations.
>
> *Section* 1. *Be it Enacted by the General Assembly of the State of Indiana,* That all bonds, notes and other

[22].—*Murray v. Charleston,* 96 U. S. 432; *Macallen v. Massachusetts,* 279 U. S. 620, 634; *United States, ex rel. v. City of Quincy,* 71 U. S. 535, 549; *Cooley's Constitutional Limitations, 8th Edition,* Vol. 1, p. 571.

evidences of indebtedness hereafter issued by the State of Indiana or by municipal corporations within the State upon which the said State or the said municipal corporations pay interest shall be exempt from taxation."

(Acts of Indiana, 1903, Chapter CLXXIX, page 322.)

Sixteen years later, when all of the tax laws of the State were codified, this section without change became Section 5 (twentieth) of Chapter 59, Acts of 1919, p. 203.

Section 5 of the 1919 Act has been amended four times since its enactment, but the twentieth paragraph, touching the exemption of municipal bonds, was not changed in any respect by these amendments until 1937. The intermediate amendments of the section were made in Section 1 (twentieth), Chapter 49, Indiana Acts 1920, p. 168; Section 6 (twentieth), Chapter 222, Indiana Acts 1921, p. 650; Section 1 (twentieth), Chapter 191, Indiana Acts 1923, p. 562. Ind. Stat. Ann. (Burns') 1933, Sec. 64-201 (twentieth).

In 1937, this exemption section was rewritten, and the clause exempting bonds from taxation, so far as pertinent here, now reads as follows:

"The following property shall be exempt from taxation:

. . .

Nineteenth. All bonds and other evidences of indebtedness hereafter issued by or in the name of any municipality or other political or civil subdivision of the State of Indiana . . . shall be exempt from taxation, *unless otherwise expressly provided by law.*" (Section 1 (nineteenth), Chapter 262, Indiana Acts 1937, page 1237.)

The Gross Income Tax Act was amended in 1937 (Ch. 117, Acts 1937), effective March 9, 1937 (Appendix B). The

amendment of the tax exemption law, set out above, became effective June 7, 1937. The 1937 amendment touching the tax exemption is the last law upon the subject.

Many statutes authorizing the issuance of bonds adopted prior to May 1, 1933 (the effective date of the Gross Income Act), contain exemptions from taxation similar in form to the 1903 Act.[23]

Since the enactment in 1933 of the gross income tax law, the Legislature has adopted statutes providing for the issuance of bonds which have included exemptions from taxation. These laws in language are similar to the original 1903 exemption law.[24]

23.—*Sanitary District Bonds,* Ch. 307, Sec. 8, Acts of 1913, as amended by Ch. 11, Sec. 4, Acts of 1919 and Ch. 100, Sec. 3, Acts of 1931, (1933 Burns 48-4108); *County Highway Bonds,* Ch. 112, Sec. 36, Acts of 1919, (1933 Burns 36-702); *Park District Bonds,* Ch. 144, Sec. 25, Acts of 1919, as amended by Ch. 42, Sec. 1, Acts of 1920 and Ch. 251, Sec. 1, Acts of 1927, (1933 Burns 48-5525); *County Library Bonds,* Ch. 120, Sec. 1½, Acts 1929, (1933 Burns 41-519); *Water Works Purchase Bonds,* Ch. 96, Sec. 12, Acts of 1921, as amended by Ch. 190, Sec. 2, Acts of 1927, (1933 Burns 48-5357); *Highway Assessment Bonds,* Ch. 262, Sec. 37, Acts of 1921, (1933 Burns 36-1437); *Sewer Bonds,* Ch. 93, Sec. 9, Acts of 1927, (1933 Burns 48-3935).

24.—*Exemption of Waterworks Bonds,* effective March 9, 1933, reading: "Said bonds shall be exempt from taxation for any and all purposes." Chapter 235, Acts of Indiana 1933, p. 1076; *Exemption of Utility Revenue Bonds,* effective March 11, 1933, reading that said bonds "shall be exempt from taxation for any and all purposes." Chapter 254, Acts of 1933, p. 1137; *Exemption of Sewage Disposal Bonds,* effective March 8, 1933, reading: "Said bonds shall be exempt from all taxation, state, county and municipal." Chapter 187, Acts of Indiana 1933, p. 924; *Exemption of Interstate Bridge Bonds,* effective March 9, 1937, reading: "The said bonds shall be exempt from taxation by the State of Indiana and by the municipalities and political subdivisions thereof." Chapter 141, Acts of Indiana 1937, p. 798.

No construction of the statutory contract may fairly be predicated upon the ground that the exemption of municipal bonds is merely a part of a larger section generally exempting property from taxation. The legislative history of the exemption refutes such a suggestion. Its existence ante-dates by sixteen years the general tax code; and similar exemptions after the date of the code, and even after the gross income tax law, have stated the exemption from taxation in the same terms. Cf. *Hale v. Iowa State Board,* 82 L. Ed., advance paging, 66, 69.

Other than in the instant case, no decision of the state Supreme Court has construed the scope and extent of statutes exempting bonds from taxation.

To Tax Gross Income from Bonds is to Tax the Bonds

Regardless of how this tax has been characterized by the state court, its operation is to impose a charge of one per cent (R. 79, 92) upon every dollar of interest received from municipal bonds declared to be tax exempt. The tax is not upon the *net result* of many transactions, but is upon *gross receipts,* and the extent of the tax varies with every dollar of interest received. The law takes one cent from every dollar received as interest on bonds. This amounts to a levy upon the bonds themselves. In *Northwestern Mutual Life Insurance Company v. Wisconsin,* 275 U. S. 136, this Court reversed a decision of the Supreme Court of Wisconsin which denied a right to the appellant to recover excess taxes paid. The law under which the tax was assessed and sought to be recovered was a license tax imposed upon life insurance companies at the rate of three per cent on *gross income,* after allowing for certain deductions. The company asserted that the law imposed a tax directly upon Federal bonds owned by it in violation of the Constitution since the law permitted

no deduction for interest derived from such bonds. The State contended as follows:

> "*Counsel for the state maintain that the effect of Sec. 76.34 is to impose upon domestic insurance companies a privilege or franchise tax, and not one on property or income;* that no charge is laid upon bonds of the United States, but the fee exacted is for *granted privileges,* including *exemption from personal property taxation and right to do business;* that the state may require domestic corporations to pay privilege, franchise or license taxes measured by gross income, although partly derived from United States bonds; and that in no proper sense can the challenged tax be regarded as one directly imposed upon gross income." (275 U. S. 139.)

The Court held that bonds of the United States were beyond the taxing power of the State. The Court said:

> ". . . it has been the settled doctrine here that where the principal is absolutely immune, no valid tax can be laid upon income arising therefrom. To tax this would amount practically to laying a burden on the exempted principal. Accordingly, if the challenged act, whatever called, really imposes a direct charge upon interest derived from United States bonds, it is pro tanto void."
>
> . . .
>
> "The distinction between an imposition, the amount of which depends upon dividends or net receipts, and one measured by gross returns is clear. *United States Glue Co. v. Oak Creek,* 247 U. S. 321, 328, and earlier opinions there cited." (275 U. S. 140.)
>
> . . .
>
> "Here the statute undertook to impose *a charge* of 3 per cent *upon every dollar of interest* received by the company from United States bonds. So much, in any event, the state took from these very receipts.

This *amounts,* we think, to *an imposition upon the bonds themselves,* and goes beyond the power of the state." (275 U. S. 141.)

Support for the argument as to the distinction between the effect of a gross receipts tax and a net income tax upon a transaction need not be elaborated at this point. In the earlier part of this brief, upon the subject of interstate commerce, this distinction which is so well stated in the *United States Glue Company Case,* referred to in the quotation *supra,* is developed. At this point it is sufficient to note that the fundamental distinction made in the interstate commerce cases is made in the cases dealing with the effect of a tax upon interest from bonds declared to be exempt from taxation or a state tax upon interest on bonds of the federal government.

The principle of the *Northwestern Mutual Life Insurance Case,* cited supra, has not been repudiated by this Court. The principle of the case is applicable with equal force on the question of impairment of contract. The tax in question bears directly upon the bonds themselves since it varies directly with the interest on the bonds, and by a parity of reasoning this case must be controlled by the *Northwestern Mutual Life Insurance Case.*

Subsequent decisions of this Court, most of them, however, dealing with net income taxes, have, either in the majority or dissenting opinion, adverted to the distinction arising in the *United States Glue Company Case* and relied upon in the *Northwestern Mutual Life Insurance Company Case.*

In the case of *National Life Insurance Company v. United States,* 277 U. S. 508, the majority of this Court held invalid an Act of Congress imposing a net income

tax upon life insurance companies. The tax was in the nature of an excise or license tax, and provided for a deduction of all interest derived from tax exempt securities, and also for a flat deduction of four per cent of "gross income," provided that the first exemption granted should be deducted from the four per cent exemption. The net result of the tax in the case presented was to allow no different exemption for a company owning municipal securities than one not owning such securities. The majority of the Court felt that the tax was directly upon the securities and therefore invalid. The Court said:

> "It is settled doctrine that *directly to tax* the income from securities amounts to taxation of the securities themselves. *Northwestern Mutual Life Insurance Co. v. Wisconsin,* 275 U. S. 136. . . ." (277 U. S. 521.)

The dissenting opinion proceeded upon the ground that the tax was valid since it was a net income tax. In this opinion was said:

> "As the tax imposed by the Act of 1921 is on net income, I should have supposed that it was settled by *Flint v. Stone Tracy Co.,* 220 U. S. 107, that the inclusion in the computation of the interest on tax-exempt bonds, like the inclusion of the receipts from exports (*William E. Peck v. Lowe,* 247 U. S. 165; *Barclay & Co. v. Edwards,* 267 U. S. 442, 447), or the inclusion in a state tax of receipts from interstate commerce (*United States Glue Co. v. Oak Creek,* 247 U. S. 321, 326; *Shaffer v. Carter,* 252 U. S. 37, 57; *Underwood Typewriter Co. v. Chamberlain,* 254 U. S. 113, 120) would not have rendered the tax objectionable." (277 U. S. 527.)
>
> . . .
>
> "I find nothing in the cases cited by the petitioner which lends support to the view that its rights have been violated. *Directly to tax the gross income from*

securities amounts, of course, to taxing the securities themselves. Northwestern Mut. L. Ins. Co. v. Wisconsin, 275 U. S. 136. . . ." (277 U. S. 532.)

Another case in which the *Northwestern Mutual Life Insurance Company Case* is cited is that of *Macallen Company v. Massachusetts,* 279 U. S. 620. In that case this Court held invalid an Act of the State of Massachusetts imposing an excise tax upon domestic corporations, so far as the Act purported to include in net income the interest on bonds of the Federal Government and of municipal corporations of Massachusetts expressly exempt by statute. The exemption section of the Massachusetts law, which is Section 5 (25) of Chapter 59 of the General Laws of Massachusetts of 1921, is in terms almost identical with the Indiana exemption act. The majority of the Court, in answer to the attack that the tax impaired the obligation of contract as applied to interest derived from tax exempt securities, said:

> ". . . bonds of Massachusetts counties and municipalities which, when issued and acquired by the corporation were exempt from taxation by the terms of a statute." (279 U. S. 624.)

The Court held:

> "We conclude that the . . . Act in substance and effect imposes a tax upon . . . the county and municipal bonds. . . . The Act is void . . . as . . . the Act impairs the obligation of the statutory contract of the State by which the bonds were made exempt from state taxation." (279 U. S. 634.)

In a dissenting opinion, the distinction between net and gross receipts taxes is noted. This opinion states:

> "The tax is not measured by gross income as in *Northwestern Mutual Life Insurance Co. v. Wisconsin,*

> 275 U. S. 136, where the validity of an excise measured by net income was recognized. The distinction between net income and gross, as the measure of a tax, is well established. *William E. Peck & Co. v. Lowe,* 247 U. S. 165; cf. *Crew Levick Co. v. Pennsylvania,* 245 U. S. 292; *United States Glue Co. v. Oak Creek,* 247 U. S. 321, 328. Being on net income, the tax does not vary in exact proportion to the gross income from the tax exempt securities included in the aggregate." (279 U. S. 635.)

The dissenting opinion concluded that since the tax was upon net income it should be held valid.

The distinction between a net and gross income tax is again referred to by this Court in the case of *Fox Film Corporation v. Doyal,* 286 U. S. 123, where the Court held valid a gross receipts tax as applied to the licensing of copyrighted moving pictures. The Court placed the holding upon the grounds that a copyright was ~~not a~~ Federal instrumentality, but at the outset of the opinion, the Court said:

> "The Gross Receipts Tax Act (Georgia Laws 1929, p. 103), describes the tax as laid 'upon the privilege of engaging in certain occupations' and 'upon certain business and commercial transactions and enterprise.' As the tax is measured by gross receipts, the case is not ruled by *Educational Films Corp. v. Ward,* 282 U. S. 379, where the tax was based upon the net income of the corporation. Appellant insists, and we think rightly, that the operation of the statute here in question, in its *application to gross receipts,* is to *impose a direct charge* upon the royalties. *Northwestern Mut. L. Ins. Co. v. Wisconsin,* 275 U. S. 136, 141; see also *Crew Levick Co. v. Pennsylvania,* 245 U. S. 292, 297; *United States Glue Co. v. Oak Creek,* 247 U. S. 321, 328, 329; *New Jersey Bell Teleph. Co. v. State Bd. of Taxes and Assessments,* 280 U. S. 338, 346. The question is thus presented whether copy-

rights are to be deemed instrumentalities of the Federal Government and hence immune from state taxation." (286 U. S. 126.)

The latest case of this Court dealing with this subject also recognizes the clear line between a gross and a net tax. In this case, the Court held valid a net income tax of the State of Iowa as applied to the interest from tax exempt municipal securities. In the case, the Court said:

> "*The tax is laid upon the net results of a bundle or aggregate of occupations and investments. Under a statute so conceived and framed a man may own a quantity of state and county bonds and pay no tax whatever. The returns from his occupation and investments are thrown into a pot, and after deducting payments for debts and expenses as well as other items, the amount of the net yield is the base on which his tax will be assessed.* Cf. *United States Glue Co. v. Oak Creek,* 247 U. S. 321, 329. In the light of all the precedents brought together in this opinion, we cannot say that a tax assessed on such a base is a plain violation of any contract of exemption to be discovered in the laws of Iowa." *Hale v. Iowa State Board of Assessment and Review,* 82 L. Ed., advanced paging, 66, 72.

The case of *Orr v. Gilman,* 183 U. S. 278, upon which the Supreme Court of Indiana relies, is not controlling upon this point. It is settled that an inheritance or succession tax is a tax upon the privilege of receiving property or, upon the privilege of transferring property at death and not upon the property transferred.

Magoun v. Illinois Trust & Savings Bank, 170 U. S. 283, 288;

Crittenberger v. State, 189 Ind. 411, 423;

See cases collected, 103 A. L. R. 81.

The gross income tax now before the Court is a *recurrent tax* that falls upon every dollar of interest from the tax exempt bonds as it is received. It is levied directly upon all interest and must be paid quarterly. An inheritance or succession tax is a sporadic tax. Bonds may even mature before it is assessed. It is never paid by the owner of the security but by his estate or his heirs after his death. It is a tax that is assessed but once in a lifetime. The *net estate* is taxed by such acts, allowance being made for debts against the appraised value of the assets of the estate. Indirect and remote is the effect of such taxation upon a contract of exemption. Direct and immediate is this gross tax which quarterly takes one cent from every dollar of interest on the exempt bonds.

The distinction that appellant here seeks to draw between the case of *Orr v. Gilman* and this case is demonstrated by the decisions of this Court. In *Snyder v. Bettman,* 190 U. S. 249, this Court held valid a Federal succession tax upon a bequest to a municipal corporation. Later, this Court held invalid an Act of Congress imposing an excise tax upon insurance companies so far as that tax included in its measure the interest from tax exempt state and municipal bonds. *National Life Insurance Company v. United States,* 277 U. S. 508. Likewise, in *Plummer v. Coler,* 178 U. S. 115, this Court held valid a state inheritance tax upon a legacy of United States bonds declared by the statute under which they were issued to be exempt from state taxation. However, this Court has held invalid a State gross receipts tax which included the interest from bonds of the United States. *Northwestern Mutual Life Insurance Co. v. Wisconsin,* 275 U. S. 136. These four cases demonstrate the practical line of distinction between a direct annual tax upon the interest from tax

exempt securities and the indirect inheritance tax on the privilege of transferring such securities at death.

> *Cf. James v. Dravo Contracting Co.*, 82 L. Ed. advance paging 125, 136, 143-144.

We respectfully submit that the Indiana tax on gross receipts impairs the admitted obligation of contract that the bonds shall be exempt from taxation, since it takes from the interest on such bonds a part of every dollar received.

Conclusion

In view of the foregoing, the decision of the Supreme Court of the State of Indiana should be reversed.

Respectfully submitted,

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February 15, 1938.

APPENDIX A

Chapter 50, Indiana Acts 1933

(Ind. Stat. Ann. (Burns) Sec. 64-2601 et seq.)

AN ACT to provide for the raising of public revenue by imposing a tax upon the receipt of gross income, to provide for the ascertainment, assessment and collection of said tax, and to provide penalties for the violation of the terms of this Act, and declaring an emergency.

Section 1. Be it enacted by the general assembly of the State of Indiana, That this Act may be cited as the "Gross Income Tax Act of 1933."

(a) When used in this Act, the term "person" or the term "company" herein used interchangeably, includes any individual, firm, copartnership, joint venture, association, corporation, municipal corporation, estate, trust, or any other group or combination acting as a unit, and the plural as well as the singular number, unless the intention to give a more limited meaning is disclosed by the context.

* * *

(f) The term "gross income," except as hereinafter otherwise expressly provided, means the gross receipts of the taxpayer received as compensation for personal services, and the gross receipts of the taxpayer derived from trades, businesses or commerce, and the gross receipts proceeding or accruing from the sale of property, tangible or intangible, real or personal, or service, or any or all of the foregoing, and all receipts by reason of the investment of capital, including interest, discount, rentals, royalties, fees, commissions or other emoluments, however designated, and without any deductions on account of the costs of property sold, the cost of materials used, labor cost, interest or discount paid, or any other expense whatsoever, and without any deductions on account of losses; Provided, however, That the term "gross income" shall not include cash discounts allowed and taken on sales; nor freight prepaid by the taxpayer and repaid to him by the purchaser; goods, wares, or merchandise, or the value thereof,

returned by customers when the sale price is refunded either in cash or by credit; nor the sale price of any article accepted as part payment on any new article sold, if and when the full sale price of the new article is included in the "gross income" subject to taxation under this Act; Provided, further, That "gross income" shall include the proceeds from the sale of any property handled on consignment by the taxpayer.

(g) In the case of banks, trust companies, building and loan associations, brokers, finance companies, dealers in commercial paper, and persons engaged in the business of lending money or credit, the term "gross income" shall be deemed to mean gross earnings in respect to that part of the total gross income of such persons which is derived from the businesses and activities enumerated in this subsection.

(h) In case of domestic insurance carriers, gross income shall not include income which becomes a reserve or other policy liability in accordance with the laws of this state or the rulings of the duly authorized supervisory officials and shall not include such premium income as is derived from business conducted outside this state on which such domestic insurance carrier pays a premium tax of one per cent or more.

Sec. 2. There is hereby imposed a tax, measured by the amount or volume of gross income, and in the amount to be determined by the application of rates on such gross income as hereinafter provided. Such tax shall be levied upon the entire gross income of all residents of the State of Indiana, and upon the gross income derived from sources within the State of Indiana, of all persons and/or companies, including banks, who are not residents of the State of Indiana, but are engaged in business in this state, or who derive gross income from sources within this state, and shall be in addition to all other taxes now or hereafter imposed with respect to particular occupations and/or activities. Said tax shall apply to, and shall be levied and collected upon, all gross incomes received on or after the first day of May, 1933, with such exceptions and limitations as may be hereinafter provided.

Sec. 3. The tax hereby provided for shall be imposed at the following rates:

(a) Upon the entire gross income of every person engaged in the business of manufacturing, compounding, or preparing for sale, profit, or use, any article or articles, substance or substances, commodity or commodities; or in the business of mining and/or producing for sale, profit, or commercial use any oil, natural gas, stone, coal, sand, gravel or other mineral product, or felling and producing timber, for sale, profit or commercial use; or in agriculture, including the production of live stock, poultry, eggs, or any other product of the farm, orchard, garden or greenhouse, one-fourth of one per cent.

(b) Upon the entire gross income of every person engaged in the business of wholesaling and/or jobbing tangible commodities not specifically mentioned in subsection (d) of this section, one-fourth of one per cent.

(c) Upon the entire gross income of every person engaged in the business of retailing of any tangible commodity or commodities not specifically mentioned in subsection (d) of this section, one per cent.

. . .

(f) Upon the gross income of every person engaged in any business or activity not enumerated in subsections (a) to (e), inclusive, of this section, including, but not in limitation of the foregoing, the gross income from professional services, personal services, sales of real estate, all funds received for the performance of contracts, all funds from the investment of capital, and all receipts from any source whatsoever, one per cent.

. . .

Sec. 5. In computing the amount of tax levied under the provisions of this Act for any year, there shall be deducted from the gross income of the taxpayer an amount of one thousand dollars. . . .

Sec. 6. There shall be excepted from the gross income taxable under this Act:

(a) So much of such gross income as is derived from business conducted in commerce between this state and other states of the United States, or between this state and foreign coun-

tries, to the extent to which the State of Indiana is prohibited from taxing under the Constitution of the United States of America. There shall also be excepted from such gross income, salaries, pensions, and other emoluments paid by the United States of America or any of its agencies, and interest or other earnings paid upon bonds or other securities issued by the United States of America or its agencies, to the extent that the State of Indiana is prohibited from imposing a tax upon such salaries, pensions, emoluments, interest and/or earnings, by the Constitution of the United States of America.

(b) All taxes received or collected by the taxpayer as agent for the State of Indiana and/or the United States of America.

(c) So much of such gross income as is derived from sales to the United States government, its departments, or agencies, to the extent to which the State of Indiana is prohibited from taxing under the Constitution of the United States of America.

(d) Amounts received under life insurance policies and contracts paid by reason of the death of the insured.

(e) Amounts received, other than amounts paid by reason of the death of the insured, under life insurance endowment or annuity contracts, either during the term, or at maturity, or upon surrender of the contract, but in no case in excess of the total amount of the premiums paid upon such contracts.

Sec. 7. There are, however, excepted from the provisions of this Act:

(a) Insurance companies which pay the State of Indiana a tax of more than one per cent upon premiums levied under the provisions of the laws of this state.

(b) Labor, agricultural and horticultural societies and other organizations not operated for profit; cemetery associations and companies which are organized and operated exclusively for the benefit of their members; fraternal benefit societies, orders or associations, operating under the lodge system for the exclusive benefit of the members, and providing

for the payment of death, sickness, accident or other benefits to the members of such societies, orders or associations, and to the dependents of such members; corporations, associations or societies organized and operated exclusively for religious, charitable, scientific, fraternal or educational purposes; business leagues, chambers of commerce, boards of trade, civic leagues and other organizations operated exclusively for the benefit of the community and for the promotion of social welfare; Provided, however, That this exception shall apply only to companies, organizations, corporations and/or societies named in this subsection which are not organized for profit, and no part of the income of which inures to the benefit of any stockholder or other private individual.

. . .

Sec. 9. (a) The taxes levied hereunder shall be due and payable in quarterly installments, on or before the fifteenth day of January, April, July and October in each year, for the period ending on the last day of the preceding month. The taxpayer shall, on or before the fifteenth day of such months, make out a return, in the form required by subsection (c) of this section, showing the amount of the tax for which he is liable, for the preceding quarter, and shall mail the same, together with a remittance for the amount of the tax, to the office of the department of treasury. . . .

. . .

Sec. 15. The tax imposed by this Act shall be in addition to all other licenses and taxes imposed by law as a condition precedent to engaging in any business taxable hereunder, except as in this Acct otherwise specifically provided. But no municipality shall be authorized to levy any tax by virtue of the provisions of this Act.

. . .

Sec. 17. On or before the fifth day of each month the total amount received from taxes levied under the provisions of this Act during the preceding month shall be paid by the department of treasury into the state treasury and credited to the general fund, and said funds shall be available for any purposes for which the legislature has made appropriations.

Sec. 25. (a) The department of treasury shall from time to time promulgate such rules and regulations not inconsistent with this Act, for making returns and for the ascertainment, assessment, and collection of the tax imposed hereunder, as it may deem necessary and desirable; and upon request shall furnish any taxpayer with a copy of such rules and regulations.

(b) All forms necessary and proper for the enforcement of this Act shall be prescribed, printed and furnished by the department of treasury.

APPENDIX B

Chapter 117, Indiana Acts 1937

(Ind. Stat. Ann. (Burns), Dec. 1937 Cum. Pocket Supp. Sec. 64-2601, *et seq.*)

AN ACT to amend Sections 1, 2 (reciting the sections and title of the Gross Income Tax Act of 1933, and of prior amendments thereto) and declaring an emergency.

Section 1. Be it enacted by the general assembly of the State of Indiana, That Section 1 of the first above entitled act be amended to read as follows: Sec. 1. That this act may be cited as the "Gross Income Tax Act of 1933."

. . .

(m) The term "gross income," except as hereinafter otherwise expressly provided, means the gross receipts of the taxpayer received as compensation for personal services, . . . and the gross receipts received from the sale, transfer, or exchange, of property, tangible of intangible, real or personal, including . . . all receipts received by reason of the investment of capital, including but not in limitation thereof, interest, discounts, . . . Provided, further, That with respect to individuals resident in Indiana and corporations incorporated under the laws of Indiana authorized to do and doing business in any other state and/or foreign country, the term "gross income" shall not include gross receipts received from sources outside the State of Indiana in cases where such gross receipts are received from a trade or business situated and regularly carried on at a legal situs outside the State of Indiana, or from activities incident thereto (including the disposal of capital assets or other properties which had been theretofore acquired or used in carrying on such trade or business). . . .